

## Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name LifeWays	County Jackson
Fiscal Year End September 30, 2007	Opinion Date April 7, 2008	Date Audit Report Submitted to State April 11, 2008	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

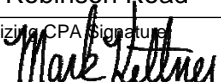
We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES ☒ NO ☐ Check each applicable box below. (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☐ ☒ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☐ ☒ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

<b>We have enclosed the following:</b>	Enclosed	Not Required (enter a brief justification)		
Financial Statements	<input checked="" type="checkbox"/>			
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>			
Other (Describe)	<input type="checkbox"/>			
Certified Public Accountant (Firm Name) REHMANN ROBSON		Telephone Number 517.787.6503		
Street Address 675 Robinson Road		City Jackson	State MI	Zip 49203
Authorizing CPA Signature 		Printed Name Mark T. Kettner, CPA, CGFM		License Number 11673

**Financial Statements  
For the Year Ended  
September 30, 2007**

**LifeWays**  
paths for personal growth

Your First Pathway to

Behavioral Health Care

in Jackson and Hillsdale



**REHMANN ROBSON**

*Certified Public Accountants*



**Jackson, Michigan**

**Financial Statements**

**For the Year Ended  
September 30, 2007**

# LifeWays

## Table of Contents

---

	<b><u>PAGE</u></b>
<b>Independent Auditors' Report</b>	1-2
<b>Management's Discussion and Analysis</b>	3-7
<b>Basic Financial Statements for the Year Ended September 30, 2007</b>	
Government-wide/Fund Financial Statements:	
Statement of Net Assets – Proprietary Funds	8
Statement of Activities and Proprietary Funds	
Revenue, Expenses, and Changes in Fund Net Assets	9
Statement of Cash Flows – Proprietary Funds	10-11
Notes to Financial Statements	12-22
<b>Required Supplementary Information</b>	
GASB Statement 25 – Employee Retirement System:	
Schedule of Funding Progress	23
Schedule of Employer Contributions	23
<b>Supplementary Information</b>	
Combining Statement of Net Assets – Internal Service Funds	24
Combining Statement of Revenue, Expenses and Changes in Fund Net Assets – Internal Service Funds	25
Combining Statement of Cash Flows – Internal Service Funds	26
<b>Internal Control and Compliance</b>	
Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	27-30

\* \* \* \* \*



# REHMANN ROBSON

*Certified Public Accountants*

A member of THE REHMANN GROUP



## **INDEPENDENT AUDITORS' REPORT**

April 7, 2008

The Board of Directors  
LifeWays  
Jackson, Michigan

We have audited the accompanying financial statements of the business-type activities, the major fund, and the aggregate remaining fund information of **LifeWays** as of and for the year ended September 30, 2007, which collectively comprise LifeWays' basic financial statements as listed in the table of contents. These financial statements are the responsibility of LifeWays' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities, the major fund, and the aggregate remaining fund information of LifeWays as of September 30, 2007, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 7, 2008, on our consideration of LifeWays' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis and GASB Statement 25 supplementary information listed in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and do not express an opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise LifeWays' basic financial statements. The combining fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Lobson". The signature is written in a cursive, flowing style with a large initial 'L'.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

## **LifeWays**

### **Management's Discussion and Analysis**

As management and administrators of LifeWays, we offer readers of LifeWays' financial statements this narrative overview and analysis of the financial activities of LifeWays for the fiscal year ended September 30, 2007.

#### **Overview of the Financial Statements**

- Total assets of LifeWays amounted to \$16,821,811 and total liabilities amounted to \$13,867,625 on September 30, 2007.
- As of the close of the current fiscal year, LifeWays' reported ending net assets of \$2,954,186.

This discussion and analysis is intended to serve as an introduction to LifeWays' basic financial statements. LifeWays' basic financial statements are comprised of two components:

- 1) Government-wide/fund financial statements
- 2) Notes to the financial statements.

This report also contains other supplementary information in addition to the basic financial statements themselves.

**Government-wide/Fund Financial Statements.** As permitted by GASB Statement No. 34, LifeWays uses an alternative approach reserved for single program governments to present combined government-wide and fund financial statements. These financial statements are designed to provide readers with a broad overview of LifeWays' finances, in a manner similar to a private-sector business. This is done by reporting LifeWays' assets and liabilities using the full accrual method of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

The *Statement of Net Assets* presents information on all of LifeWays' assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of LifeWays is improving or deteriorating.

The *Statement of Activities and Proprietary Fund Revenue, Expenses and Changes in Fund Net Assets* presents information showing how LifeWays' revenue and expenses changed during the most recent fiscal year. All changes in revenue and expenses are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods. In addition, this statement discloses *non-cash* expenditures of depreciation and amortization, which affect the ending book value of capital assets.



The *Statement of Cash Flows* presents information about the source and usage of cash and cash equivalents and divides the information reported into three classifications: operating, financing, and investing. LifeWays' operations generate and use cash in the normal flow of activity: the collection of revenues and payments to contractors plus the non-cash activity add-backs such as depreciation. Financing activities include borrowing and repayment of long-term debt and the purchase of capital assets. Investing includes such items as investment of cash and other long-term assets.

**Notes to the financial statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide/fund financial statements. The accompanying notes are an integral part of the financial statements and must be reviewed in conjunction with the information reported on the financial statements to provide a full understanding of LifeWays' financial situation.

### **Government-wide Financial Analysis**

The largest portion of LifeWays' total assets (\$12,742,227 or 76%) reflects its investment in capital asset at 1200 N West Avenue, group homes, equipment and furniture.

#### **LifeWays' Total Assets & Net Assets**

	<b><u>2006</u></b>	<b><u>2007</u></b>
Current and other assets	\$ 9,771,831	\$ 4,079,584
Capital assets, net	<u>10,622,375</u>	<u>12,742,227</u>
<b>Total assets</b>	<b><u>20,394,206</u></b>	<b><u>16,821,811</u></b>
Long-term liabilities outstanding	10,557,440	10,228,704
Other liabilities	<u>3,760,912</u>	<u>3,647,921</u>
<b>Total liabilities</b>	<b><u>14,318,352</u></b>	<b><u>13,867,625</u></b>
Net assets:		
Invested in capital assets, net of related debt	64,935	2,513,523
Restricted	1,625,357	656,891
Unrestricted	<u>4,385,562</u>	<u>(216,228)</u>
<b>Total net assets</b>	<b><u>\$ 6,075,854</u></b>	<b><u>\$ 2,954,186</u></b>

LifeWays' net assets decreased by \$3,121,668 during the current fiscal year. This reduction in fund balances was invested in additional services to consumers as well as financing the purchase and renovation of building at 1200 N West Avenue.

## LifeWays' Changes in Net Assets

	<u>2006</u>	<u>2007</u>
<b>Operating revenue:</b>		
MDCH Contract – Medicaid & General Funds	\$ 36,121,640	\$ 37,367,524
Operating grants and contributions	1,742,584	3,823,234
Charges for services and other local revenue	<u>755,976</u>	<u>1,093,479</u>
	<u>38,620,200</u>	<u>42,284,137</u>
<b>Operating expenses:</b>		
Board administration	4,287,355	4,514,143
Mental health services	34,074,811	39,713,168
Substance abuse	650,919	563,322
Depreciation and amortization	<u>191,431</u>	<u>242,678</u>
	<u>39,204,516</u>	<u>45,033,311</u>
<b>Operating income (loss)</b>	<b>(584,316)</b>	<b>(2,749,174)</b>
<b>Non-operating revenue (expense)</b>		
Prior year cost settlement	(15,293)	(77,995)
Interest income	397,334	297,989
Interest expense	<u>(197,656)</u>	<u>(602,235)</u>
	<u>184,385</u>	<u>(382,241)</u>
<b>Net income (loss)</b>	<b>(399,931)</b>	<b>(3,131,415)</b>
Net assets, beginning of year, as restated	<u>6,475,785</u>	<u>6,085,601</u>
<b>Net assets, end of year</b>	<b><u>\$ 6,075,854</u></b>	<b><u>\$ 2,954,186</u></b>

### **Financial Analysis of LifeWays' Funds**

As noted earlier, LifeWays uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Operating Fund.** LifeWays accounts for its primary operations in an enterprise fund which is accounted for on the same basis of accounting as the government-wide financial statements. Accordingly, a separate analysis is not included herein. For several years LifeWays had been building up a pool of reserve funds from excess annual revenue. Resulting from a policy change in how MDCH makes revenue determination, LifeWays decided to invest greater portion of its annual revenue in service delivery, hence halting annual contribution to fund balances.

**Internal Service Funds.** LifeWays' internal service funds are used to account for assets held as a reserve against potential liabilities relative to and allowed by its contract with the Michigan Department of Community Health (MDCH). LifeWays' risk management plan has been reviewed and approved by LifeWays board of directors and MDCH.

## **Capital Asset and Debt Administration**

**Capital assets.** LifeWays' investment in capital assets for its activities as of September 30, 2007, amounted to \$12,742,227 (net of accumulated depreciation of \$1,564,411). This investment in capital assets includes administrative, Provider offices and retail building, group homes, leasehold improvements, and equipment. Capital assets increased by \$2,119,852 during the current fiscal year.

Accumulated depreciation at September 30, 2007 amounted to \$1,564,411 and included current year depreciation expense of \$235,598. The increase in depreciation expense is due to the fact the LifeWays now owns its administrative offices at 1200 N West.

### **LifeWays' Capital Assets**

(Net of depreciation)

September 30, 2007

Land	\$ 2,000,000
Buildings	9,354,557
Computer equipment	24,496
Furnishings and other equipment	145,065
Leasehold improvements	499,168
Group homes	<u>718,941</u>
<b>Total</b>	<b><u>\$12,742,227</u></b>

**Long-term debt.** At the end of the current fiscal year, LifeWays had general obligation bond and commercial mortgage debt outstanding of \$10,228,704 (net of discount). The repayment due in next fiscal year is \$378,736. These bonds were issued to finance the acquisition of five group homes for providing residential services to LifeWays' consumers and to purchase and renovate the LifeWays office at 1200 N West Avenue. LifeWays uses the rental income from leased space to service bonds and mortgage payments.

### **Factors Bearing on LifeWays' Future**

The following factors were considered in preparing LifeWays' budget for the 2007-08 fiscal year:

- Reduction in administration costs
- Increase costs associated with being a landlord for premises at 1200 N West Avenue.
- Increases in known and estimated costs – namely, energy, health insurance, workers' compensation insurance and salary increases.
- An increasing trend in Medicaid-eligible consumers and the uninsured population related to increased unemployment and a sluggish economy.
- Revenue generation from non traditional sources.
- Potential Federal and State Medicaid and general Funds cuts either through funding or service eligibility.
- Maintain consumer service expenses within budget and MDCH benchmarks
- Increased demand for state and community in-patient services.
- New community service initiatives including:
  - ✓ Investment in services to children and persons with substance abuse diagnosis
  - ✓ Service integration initiatives for dually diagnosed Consumers

LifeWays moving away from holding larger fund balances to investing in real estate has translated into foregoing short-term interest income for long term rental income. The financial payoff of this decision will not be realized for several years when LifeWays has greater equity in the group homes and administrative properties.

### **Requests for Information**

This financial report is designed to provide a general overview of LifeWays' finances for all those with an interest in LifeWays' finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Ivan Gibbs, Chief Finance Officer, LifeWays 1200 N. West Ave. Jackson, Michigan 49202.

## **BASIC FINANCIAL STATEMENTS**

**LifeWays**  
**Statement of Net Assets**  
**Proprietary Funds**  
**September 30, 2007**

	<u>Enterprise Operating Fund</u>	<u>Internal Service Funds</u>	<u>Total Business-type Activities</u>
<b>Assets</b>			
Cash and cash equivalents	\$ 1,628,167	\$ 656,891	\$ 2,285,058
Receivables:			
Fees, net of allowance for doubtful accounts of \$49,604	79,912	-	79,912
Due from Michigan Department of Community Health	1,355,611	-	1,355,611
Other	208,493	-	208,493
Prepaid items	64,358	-	64,358
Capital assets not being depreciated	2,000,000	-	2,000,000
Capital assets being depreciated, net	10,742,227	-	10,742,227
Unamortized bond issuance costs	86,152	-	86,152
	<hr/>	<hr/>	<hr/>
Total assets	16,164,920	656,891	16,821,811
	<hr/>	<hr/>	<hr/>
<b>Liabilities</b>			
Accounts payable	2,316,923	-	2,316,923
Due to Michigan Department of Community Health	164,634	-	164,634
Accrued liabilities	234,862	-	234,862
Claims incurred but not reported	922,502	-	922,502
Long-term debt:			
Due within one year	378,736	-	378,736
Due in more than one year	9,849,968	-	9,849,968
	<hr/>	<hr/>	<hr/>
Total liabilities	13,867,625	-	13,867,625
	<hr/>	<hr/>	<hr/>
<b>Net assets</b>			
Invested in capital assets, net of related debt	2,513,523	-	2,513,523
Restricted for contract losses	-	656,891	656,891
Unrestricted (deficit)	(216,228)	-	(216,228)
	<hr/>	<hr/>	<hr/>
Total net assets	\$ 2,297,295	\$ 656,891	\$ 2,954,186
	<hr/>	<hr/>	<hr/>

The accompanying notes are an integral part of these financial statements.

**LifeWays**  
**Statement of Activities and**  
**Proprietary Fund Revenue, Expenses, and Changes in Fund Net Assets**  
**For the Year Ended September 30, 2007**

	<u>Enterprise</u> <u>Operating</u> <u>Fund</u>	<u>Internal</u> <u>Service</u> <u>Funds</u>	<u>Adjustments</u>	<u>Total</u> <u>Business-type</u> <u>Activities</u>
<b>Operating revenue</b>				
Medicaid capitation	\$ 30,813,812	\$ -	\$ -	\$ 30,813,812
State general fund indigent	6,027,735	-	-	6,027,735
Earned revenues, grants and federal programs	3,823,234	-	-	3,823,234
Substance abuse	525,977	-	-	525,977
Local revenue:				
County appropriations	94,136	-	-	94,136
Rental revenue	455,331	-	-	455,331
First party	4,154	-	-	4,154
Third party	350,189	-	-	350,189
Other local revenue	146,446	43,123	-	189,569
	<u>42,241,014</u>	<u>43,123</u>	<u>-</u>	<u>42,284,137</u>
<b>Total operating revenue</b>				
	42,241,014	43,123	-	42,284,137
<b>Operating expenses</b>				
Board administration	4,514,143	-	-	4,514,143
Mental health services	39,713,168	-	-	39,713,168
Substance abuse	563,322	-	-	563,322
Depreciation and amortization	242,678	-	-	242,678
	<u>45,033,311</u>	<u>-</u>	<u>-</u>	<u>45,033,311</u>
<b>Total operating expenses</b>				
	45,033,311	-	-	45,033,311
<b>Operating income (loss)</b>				
	<u>(2,792,297)</u>	<u>43,123</u>	<u>-</u>	<u>(2,749,174)</u>
<b>Non-operating revenue (expense)</b>				
Prior year cost settlement	(77,995)	-	-	(77,995)
Interest income	210,040	87,949	-	297,989
Interest expense	(602,235)	-	-	(602,235)
	<u>(470,190)</u>	<u>87,949</u>	<u>-</u>	<u>(382,241)</u>
<b>Total non-operating revenue</b>				
	(470,190)	87,949	-	(382,241)
<b>Net income (loss) before transfers</b>				
	(3,262,487)	131,072	-	(3,131,415)
<b>Transfers in</b>	1,099,538	-	(1,099,538)	-
<b>Transfers out</b>	<u>-</u>	<u>(1,099,538)</u>	<u>1,099,538</u>	<u>-</u>
<b>Change in net assets</b>				
	(2,162,949)	(968,466)	-	(3,131,415)
<b>Net assets, beginning of year, as restated</b>	<u>4,460,244</u>	<u>1,625,357</u>	<u>-</u>	<u>6,085,601</u>
<b>Net assets, end of year</b>	<u>\$ 2,297,295</u>	<u>\$ 656,891</u>	<u>\$ -</u>	<u>\$ 2,954,186</u>

The accompanying notes are an integral part of these financial statements.

**LifeWays**  
**Statement of Cash Flows**  
**Proprietary Funds**  
**For the Year Ended September 30, 2007**

	<u>Enterprise Operating Fund</u>	<u>Internal Service Funds</u>
<b>Cash flows from operating activities</b>		
Cash received from customers and others	\$ 40,985,644	\$ 43,123
Cash payments to employees	(3,371,638)	-
Cash payments to suppliers for goods and services	(41,441,484)	-
	<u>(3,827,478)</u>	<u>43,123</u>
<b>Net cash provided by (used in) operating activities</b>		
	<u>(3,827,478)</u>	<u>43,123</u>
<b>Cash flows from capital and related financing activities</b>		
Principal paid on bonds	(330,880)	-
Interest paid on bonds	(602,235)	-
Purchase of capital assets	(2,355,450)	-
	<u>(3,288,565)</u>	<u>-</u>
<b>Net cash used in capital and related financing activities</b>		
	<u>(3,288,565)</u>	<u>-</u>
<b>Cash flows from non-capital financing activities</b>		
Transfers in	1,099,538	-
Transfers out	-	(1,099,538)
	<u>1,099,538</u>	<u>(1,099,538)</u>
<b>Net cash provided by (used in) non-capital financing activities</b>		
	<u>1,099,538</u>	<u>(1,099,538)</u>
<b>Cash flows from investing activities</b>		
Interest received	210,040	87,949
	<u>210,040</u>	<u>87,949</u>
<b>Net decrease in cash and cash equivalents</b>		
	<u>(5,806,465)</u>	<u>(968,466)</u>
Cash and cash equivalents, beginning of year, as restated	7,434,632	1,625,357
	<u>7,434,632</u>	<u>1,625,357</u>
<b>Cash and cash equivalents, end of yea</b>	<u>\$ 1,628,167</u>	<u>\$ 656,891</u>

continued...



**LifeWays**  
**Statement of Cash Flows**  
**Proprietary Funds (Concluded)**  
**For the Year Ended September 30, 2007**

	<u>Enterprise Operating Fund</u>	<u>Internal Service Funds</u>
<b>Reconciliation of operating income (loss) to net cash used in operating activities</b>		
Operating income (loss)	\$ (2,792,297)	\$ 43,123
Adjustments to reconcile operating income (loss) to net cash used in operating activities:		
Depreciation and amortization	242,678	-
Prior year cost settlement	(77,995)	-
Changes in assets and liabilities:		
Fees receivable	38,847	-
Due from Michigan Department of Community Health	(1,005,879)	-
Other receivables	(119,112)	-
Prepaid items	8,271	-
Accounts payable	11,459	-
Due to Michigan Department of Community Health	(207,840)	-
Accrued liabilities	(190,412)	-
Claims incurred but not reported	356,033	-
Unearned revenue	(91,231)	-
	<u>\$ (3,827,478)</u>	<u>\$ 43,123</u>
Net cash provided by (used in) operating activities	<u>\$ (3,827,478)</u>	<u>\$ 43,123</u>

The accompanying notes are an integral part of these financial statements.

## **NOTES TO FINANCIAL STATEMENTS**

# LifeWays

## Notes to Financial Statements

---

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of **LifeWays**, a Community Mental Health Authority established under Section 205 of the Michigan Mental Health Code, have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Government Accounting Standards Board (GASB) is the accepted standards-setting body for establishing governmental accounting and financial reporting principles. The more significant of LifeWays accounting policies are described below.

#### A. Reporting Entity

As indicated above, LifeWays is a Community Mental Health Authority serving the mental health needs of Jackson and Hillsdale County residents. Its Board of Directors is appointed by the County Commissions of Jackson and Hillsdale Counties.

#### B. Government-wide and Fund Financial Statements

As permitted by GASB Statement No. 34, LifeWays uses an alternative approach reserved for single program governments to present combined government-wide and fund financial statements by using a columnar format that reconciles individual line items of fund financial data to government-wide data in a separate column. Accordingly, this is presented in the Statement of Net Assets – Proprietary Funds and the Statement of Activities and Proprietary Fund Revenues, Expenses and Changes in Fund Net Assets. LifeWays' only major fund is reported in a separate column in the aforementioned financial statements.

The operations of LifeWays are accounted for as an Enterprise Fund (a proprietary fund type) which is designed to be self-supporting. Enterprise Funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the cost of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The Risk Reserve Funds (all of which are internal service funds, a proprietary fund type) are used to account for assets held as a reserve against potential liabilities relative to and as allowed by its contract with the Michigan Department of Community Health (MDCH). Pursuant to these contractual provisions, LifeWays' risk management plan has been reviewed and approved by MDCH. Separate risk reserves are maintained for mental health and substance abuse services.

# LifeWays

## Notes to Financial Statements

---

### **C. Measurement focus, basis of accounting, and financial statement presentation**

The government-wide and proprietary fund financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The enterprise fund is LifeWays' primary operating fund, and only major fund. It accounts for all financial resources of the government, except those required to be accounted for in another fund.

Private sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to the same limitation. The government has elected not to follow subsequent private-sector guidance.

Proprietary funds distinguish *operating* revenues and expenses from *non-operating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of LifeWays' operating fund are contract revenues from MDCH, county appropriations, and first and third party billings. Operating revenues of the internal service funds are primarily comprised of charges to other funds and governmental entities for risk financing. Operating expenses include the cost of providing mental health and substance abuse services. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

### **D. Assets, liabilities and equity**

#### ***1. Deposits***

Cash and cash equivalents are considered to be cash on hand, amounts in demand deposit accounts, and amounts on deposit with the Jackson County Treasurer.

State statutes authorize units of local government to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

# LifeWays

## Notes to Financial Statements

---

### **2. *Receivables and Payables***

Fee accounts receivable are shown net of an allowance for uncollectibles, which is based on management's estimate using collection history trends.

### **3. *Prepaid Items***

Payments made to vendors for services that will benefit periods beyond September 30, 2007, are recorded as "prepaid items" in the accompanying statement of net assets.

### **4. *Capital Assets***

Capital assets are capitalized and reported in the operating fund, net of accumulated depreciation. The Authority defines capital assets as assets with an initial individual cost of at least \$5,000 and an estimated useful life of at least three years. Capital assets are depreciated on the straight-line basis over the estimated useful lives of those assets, which range from five to forty years. All purchased capital assets are recorded at cost where historical records are available and at estimated historical costs where no historical records exist. Donated capital assets, if any, are valued at their estimated fair market value on the date received.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements are capitalized.

### **5. *Compensated Absences***

Vacation, sick leave and personal days cannot be carried over, and are not accrued in the accompanying financial statements.

### **6. *Unearned Revenue***

Unearned revenue, if any, represents that portion of the current-year MDCH contract amount that may be carried-over to and expended in subsequent fiscal years. Such carryover is generally limited to five percent of the MDCH contract amount.

Medicaid savings are considered local funds under the contract with MDCH, and may be spent over a period of several years in accordance with a Medicaid Reinvestment Strategy. State General Funds carried over must generally be spent in the following year.

# LifeWays

## Notes to Financial Statements

---

### 7. Risk Management

LifeWays is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and injuries to employees. During the year ended September 30, 2007, the entity carried commercial insurance to cover all risks of losses, except for any potential operating shortfalls under the terms of its contract with MDCH, which are covered by the Risk Reserve Internal Service Funds. LifeWays had no settled claims resulting from these risks that exceeded their commercial coverage in any of the past three fiscal years.

## 2. DETAILED NOTES ON ALL FUNDS

### A. Deposits

At year end, LifeWays' cash and cash equivalents consisted of the following:

Bank deposits - checking accounts	\$ 195,429
Deposits with Jackson County Treasurer	2,089,229
Cash on hand	<u>400</u>
	<b><u>\$ 2,285,058</u></b>

LifeWays' demand accounts are comprised of checking accounts with local banks with combined bank balances of \$386,155, of which \$264,290 was uninsured and uncollateralized.

As an Authority, LifeWays is authorized to deposit or invest in any accounts or institutions as permitted by State statutes. However, because of favorable terms, LifeWays has chosen to participate in Jackson County's investment pool, which is managed by the Jackson County Treasurer. These funds are deposited in the Treasurer's pooled accounts, and are in the name of the Jackson County Treasurer. Other County funds are also deposited in those accounts and, as such, because of the complexities of FDIC Regulation #330.8, it is not possible to readily determine the amount of insurance that would be allocated to LifeWays' deposits.

# LifeWays

## Notes to Financial Statements

### B. Due From/To Michigan Department of Community Health

For the year ended September 30, 2007, the operations of LifeWays were conducted under the terms and conditions of its contract with the MDCH.

The \$1,355,611 due from the MDCH represents amounts due for the prisoner reentry initiative and other services provided by LifeWays. The receivable balance is comprised wholly of federal and state grants.

The \$164,634 due to the MDCH represents LifeWays' estimate of amounts payable to the State of Michigan for institutional care services provided by State institutions.

### C. Capital Assets

Following is a summary of capital assets activity for the year ended September 30, 2007:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets not being depreciated				
Land	\$ 2,000,000	\$ -	\$ -	\$ 2,000,000
Construction in progress	1,000,162	-	(1,000,162)	-
Total capital assets not being depreciated	<u>3,000,162</u>	<u>-</u>	<u>(1,000,162)</u>	<u>2,000,000</u>
Capital assets being depreciated				
Buildings	6,361,244	3,198,927	-	9,560,171
Computer equipment	796,093	11,254	-	807,347
Furnishings and other equipment	35,727	145,431	-	181,158
Leashold improvements	842,947	-	-	842,947
Group homes	915,015	-	-	915,015
Total capital assets being depreciated	<u>8,951,026</u>	<u>3,355,612</u>	<u>-</u>	<u>12,306,638</u>
Less accumulated depreciation for				
Buildings	53,010	152,604	-	205,614
Computer equipment	759,423	23,428	-	782,851
Furnishings and other equipment	33,652	2,441	-	36,093
Leashold improvements	312,797	30,982	-	343,779
Group homes	169,931	26,143	-	196,074
Total accumulated depreciation	<u>1,328,813</u>	<u>235,598</u>	<u>-</u>	<u>1,564,411</u>
Total capital assets being depreciated - net	<u>7,622,213</u>	<u>3,120,014</u>	<u>-</u>	<u>10,742,227</u>
Capital assets - net	<u>\$ 10,622,375</u>	<u>\$ 3,120,014</u>	<u>\$ (1,000,162)</u>	<u>\$ 12,742,227</u>

# LifeWays

## Notes to Financial Statements

### D. Long-term Debt

*Leases Payable.* The Jackson County Building Authority leases payable are equal to the aggregate outstanding principal payments due on bonds issued by the Jackson County Building Authority, that pledge the full faith and credit of the government. Those bonds were issued to finance the acquisition of five group homes for providing residential services (Series 1999 A) and to purchase and renovate the administrative building (Series 2006 A).

*Mortgage Payable.* During the year ended September 30, 2006, LifeWays borrowed \$2,800,000 under a mortgage agreement to finance the purchase and renovation of the portion of the administrative building leased to other entities.

Long-term debt currently outstanding is as follows:

	<u>Interest Rate</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Series 1999 A Jackson County Building Authority Bonds (lease payable)	4.0 - 6.0%	\$ 775,000	\$ -	\$ 50,000	\$ 725,000	\$ 50,000
Series 2006 A Jackson County Building Authority Bonds (lease payable)	4.75 - 5.0%	7,045,000	-	200,000	6,845,000	250,000
Mortgage payable	7.23%	<u>2,779,780</u>	<u>-</u>	<u>80,880</u>	<u>2,698,900</u>	<u>80,880</u>
Subtotal		10,599,780	-	330,880	10,268,900	380,880
Series 2006 A Jackson County Building Authority Bonds (debt discount)		<u>(42,340)</u>	<u>-</u>	<u>(2,144)</u>	<u>(40,196)</u>	<u>(2,144)</u>
Total		<u>\$ 10,557,440</u>	<u>\$ -</u>	<u>\$ 328,736</u>	<u>\$ 10,228,704</u>	<u>\$ 378,736</u>



# LifeWays

## Notes to Financial Statements

The requirements to amortize all debt outstanding at September 30, 2007, are as follows:

<b>Year Ending September 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2008	\$ 380,880	\$ 574,910	\$ 955,790
2009	380,880	554,538	935,418
2010	405,880	534,165	940,045
2011	405,880	512,555	918,435
2012	405,880	490,895	896,775
2013-2017	4,219,500	3,615,663	7,835,163
2018-2022	2,125,000	802,250	2,927,250
2023-2026	1,945,000	249,000	2,194,000
<b>Total</b>	<b>\$ 10,268,900</b>	<b>\$ 7,333,976</b>	<b>\$ 17,602,876</b>

*Interest Rate Swap.* During the year ended September 30, 2006, the Authority entered into an interest rate swap agreement (the “Swap”) to modify interest rates in connection with its mortgage payable, which had an original issuance amount that matched the notional amount of \$2,800,000. The notional amount of the swap declines according to the amortization schedule of the mortgage payable. The swap was entered into at the same time the mortgage was issued (June 30, 2006). The stated termination date of the Swap is June 30, 2013. Under the terms of the Swap, the Authority effectively pays interest calculated at a fixed rate of 7.23% to the lender, Citizens Bank.

# LifeWays

## Notes to Financial Statements

---

### E. Risk Reserve Fund Net Assets

At September 30, 2007, the net assets of the Risk Reserve Internal Service Funds were comprised of the following:

	<b><u>Mental Health</u></b>	<b><u>Substance Abuse</u></b>	<b><u>Total</u></b>
Beginning balance	\$1,625,357	\$ -	\$1,625,357
Additions	86,842	44,230	131,072
Deletions	<u>(1,063,584)</u>	<u>(35,954)</u>	<u>(1,099,538)</u>
<b>Ending balance</b>	<b><u>\$ 648,615</u></b>	<b><u>\$ 8,276</u></b>	<b><u>\$ 656,891</u></b>

#### ***Mental Health Risk Reserve***

Under the terms of its managed specialty supports and services contract with MDCH, LifeWays is at risk for its operating expenses in excess of contract revenues within a specified risk corridor. In accordance with the contract, LifeWays is authorized and required to retain these funds until needed to offset actual operating losses within the risk corridor. LifeWays maximum risk exposure under the contract with MDCH is \$2,896,387 based on current funding levels (\$2,339,213 Medicaid, \$448,940 general fund, and \$108,234 local).

#### ***Substance Abuse Risk Reserve***

Net assets in the substance abuse risk reserve are held on behalf of the Mid-South Substance Abuse Coordinating Agency. Contributions are made to the reserve by Mid-South as funding permits, and LifeWays distributes funds to Mid-South upon request. During the year ended September 30, 2007, the Authority received a contribution in the amount of \$43,123 from Mid-South and made a distribution in the amount of \$35,954.

# LifeWays

## Notes to Financial Statements

---

### F. Retirement Plan

LifeWays has a single-employer defined benefit pension plan (the “LifeWays Pension Plan”) for employees of LifeWays, which provides retirement, death and disability benefits covering substantially all of LifeWays’ full-time employees. Membership of the Plan consisted of the following at October 1, 2006, the date of the latest actuarial valuation:

Retirees and beneficiaries receiving benefits	10
Terminated plan members entitled to but not yet receiving benefits	62
Active plan members	<u>46</u>
	<u><b>118</b></u>

The Plan is non-contributory for employees; by Board Resolution, LifeWays is required to contribute at an actuarially determined rate all amounts necessary to provide assets sufficient to pay for member benefits. LifeWays’ contribution to the Plan for the year ended September 30, 2007, represents 15.6% of the annual covered payroll.

The Plan is administered by a third-party insurance company. Administrative costs of the Plan are financed through investment earnings.

Plan provisions are established and amended under the authority of LifeWays’ Board. Contribution requirements are established and amended subject to Board approval.

The Plan’s annual retirement benefits cost and net retirement benefits obligation for the current year were as follows:

Annual required contribution / retirement benefit cost	\$352,283
Contribution made	<u>(352,283)</u>
Increase (decrease) in net retirement benefit obligation	-
Net retirement benefit obligation, beginning of year	<u>-</u>
<b>Net retirement benefit obligation, end of year</b>	<u><b>\$ -</b></u>

The annual required contribution for the current year was determined as part of an actuarial valuation of the Plan as of September 30, 2006, using the aggregate actuarial cost method. The actuarial assumptions included: (a) a rate of return on investments of 7%; (b) projected salary increases of 2.5% attributable to inflation; and (c) the assumption that the excess of the present value of benefits over valuation assets is spread over the average working lifetime of plan participants.

# LifeWays

## Notes to Financial Statements

---

The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a four-year period. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis over 30 years from April 15, 1992.

### Three-Year Trend Information

<u>Year Ending</u>	<u>Annual Retirement Benefit Cost (ARBC)</u>	<u>Percentage of ARBC Contributed</u>	<u>Net Retirement Benefit Obligation</u>
9/30/2005	\$319,818	100.0%	\$ -
9/30/2006	353,321	100.0%	-
9/30/2007	352,283	100.0%	-

GASB Statement 25 required supplementary information is presented after the Notes to Financial Statements section of this report.

### **G. Claims Incurred But Not Reported**

LifeWays estimates the liability for contractual services provided by its contract providers that have been incurred through the end of the fiscal year, including both those claims that have been reported as well as those that have not yet been reported. Changes in the estimated liability are as follows:

Estimated liability, beginning of year	\$ 566,469
Estimated claims incurred	14,548,417
Claim payments	<u>(14,192,384)</u>
<b>Estimated liability, end of year</b>	<b><u>\$ 922,502</u></b>

# LifeWays

## Notes to Financial Statements

---

### **H. Contribution to the King Trust Charitable Gift Fund**

In 2002, LifeWays made contributions to the King Trust Charitable Gift Fund (the “Fund”) to establish the “LifeWays Foundation” account. While LifeWays may make recommendations regarding the use of the Fund, any contributions made are irrevocable and become assets of the Fund. Since LifeWays is not the trustee of the LifeWays Foundation account, and does not exercise any control over the Fund’s assets, no amounts were recorded in these financial statements at year end. The balance in the LifeWays Foundation account at September 30, 2007 was \$7,359.

### **I. Contingencies**

Under the terms of various federal and state grants and regulatory requirements, LifeWays is subject to periodic audits of its agreements. Such audits could lead to questioned costs and/or requests for reimbursement to grantor or regulatory agencies. Management does not consider such amounts to be significant.

As is the case with other entities, LifeWays faces exposure from potential claims and legal proceedings involving environmental and other matters. No such claims or proceedings have been asserted as of September 30, 2007.

### **J. Restatements**

Beginning net assets of the Operating Fund were decreased by \$9,747 to eliminate unsupported assets improperly recognized in prior periods.

\* \* \* \* \*

## **REQUIRED SUPPLEMENTARY INFORMATION**

**LifeWays**  
**GASB Statement 25 Required Supplementary Information**  
**Employee Retirement System**

**Schedule of Funding Progress**

	(1)	(2)	(3)	(4)	(5)	(6)
<b>Actuarial Valuation Date Oct. 1</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Accrued Liability (AAL) Entry Age</b>	<b>Unfunded AAL (UAAL) (2-1)</b>	<b>Funded Ratio (1/2)</b>	<b>Covered Payroll</b>	<b>UAAL as a % of Covered Payroll (3/5)</b>
1997	\$ 1,382,713	\$ 1,814,743	\$ 432,030	76.2 %	\$ 2,840,510	15.2 %
1998	1,445,894	2,222,694	776,800	65.1	2,464,317	31.5
1999	1,809,122	2,380,312	571,190	76.0	2,576,654	22.2
2000	2,236,469	2,793,508	557,039	80.1	2,271,312	24.5
2001	2,157,775	2,349,783	192,008	91.8	2,337,520	8.2
2002	2,214,182	2,708,063	493,881	81.8	1,948,381	25.3
2003	2,775,533	3,617,533	842,000	76.7	1,940,994	43.4
2004	3,401,945	3,975,950	574,005	85.6	2,197,653	26.1
2005	3,844,328	4,417,267	572,939	87.0	2,294,787	25.0
2006	4,292,667	4,858,767	566,100	88.3	2,253,345	25.1

**Schedule of Employer Contributions**

<b>Fiscal Year Ended Sept. 30</b>	<b>Annual Required Contribution</b>	<b>Annual Actual Contribution</b>	<b>Percentage Contributed</b>
1998	\$ 230,891	\$ 230,891	100.0 %
1999	303,890	303,890	100.0
2000	280,974	280,974	100.0
2001	255,090	255,090	100.0
2002	310,429	310,429	100.0
2003	336,528	336,528	100.0
2004	319,537	319,537	100.0
2005	319,818	319,818	100.0
2006	353,321	353,321	100.0
2007	352,283	352,283	100.0

## **SUPPLEMENTARY INFORMATION**



**LifeWays**  
**Combining Statement of Net Assets - Internal Service Funds**  
**September 30, 2007**

	<u>Mental Health Risk Reserve</u>		<u>Substance</u>	
	<u>Medicaid</u>	<u>General</u>	<u>Abuse</u>	
		<u>Fund</u>	<u>Risk Reserve</u>	<u>Totals</u>
<b>Assets</b>				
Cash and cash equivalents	\$ 630,053	\$ 18,562	\$ 8,276	\$ 656,891
<b>Liabilities</b>				
Unearned revenue	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Net assets</b>				
Restricted for contract losses	<u>\$ 630,053</u>	<u>\$ 18,562</u>	<u>\$ 8,276</u>	<u>\$ 656,891</u>

**LifeWays**  
**Combining Statement of Revenue, Expenses and Changes**  
**in Net Assets - Internal Service Funds**  
**For the Year Ended September 30, 2007**

	<u>Mental Health Risk Reserve</u>		<u>Substance</u>	
	<u>Medicaid</u>	<u>General</u>	<u>Abuse</u>	
		<u>Fund</u>	<u>Risk Reserve</u>	<u>Totals</u>
<b>Operating revenue</b>				
Charges for services	\$ -	\$ -	\$ 43,123	\$ 43,123
<b>Non-operating revenue</b>				
Interest income	<u>84,357</u>	<u>2,485</u>	<u>1,107</u>	<u>87,949</u>
Net income before transfers	84,357	2,485	44,230	131,072
<b>Transfers out</b>	<u>(964,047)</u>	<u>(99,537)</u>	<u>(35,954)</u>	<u>(1,099,538)</u>
Change in net assets	(879,690)	(97,052)	8,276	(968,466)
Net assets, beginning of year	<u>1,509,743</u>	<u>115,614</u>	<u>-</u>	<u>1,625,357</u>
<b>Net assets, end of year</b>	<u><u>\$ 630,053</u></u>	<u><u>\$ 18,562</u></u>	<u><u>\$ 8,276</u></u>	<u><u>\$ 656,891</u></u>

**LifeWays**  
**Combining Statement of Cash Flows**  
**Internal Service Funds**  
**For the Year Ended September 30, 2007**

	<u>Mental Health Risk Reserve</u>	<u>General</u>	<u>Substance</u>	
	<u>Medicaid</u>	<u>Fund</u>	<u>Abuse</u>	
			<u>Risk Reserve</u>	<u>Totals</u>
<b>Cash flows from operating activities</b>				
Cash payments to vendors and others	\$ -	\$ -	\$ 43,123	\$ 43,123
Cash received from interfund services	-	-	-	-
	-	-	-	-
Net cash provided by operating activities	-	-	43,123	43,123
<b>Cash flows from non-capital financing activities</b>				
Transfers out	(964,047)	(99,537)	(35,954)	(1,099,538)
<b>Cash flows from investing activities</b>				
Interest received	84,357	2,485	1,107	87,949
	84,357	2,485	1,107	87,949
Net increase (decrease) in cash and cash equivalents	(879,690)	(97,052)	8,276	(968,466)
Cash and cash equivalents, beginning of year	1,509,743	115,614	-	1,625,357
	1,509,743	115,614	-	1,625,357
<b>Cash and cash equivalents, end of year</b>	<u>\$ 630,053</u>	<u>\$ 18,562</u>	<u>\$ 8,276</u>	<u>\$ 656,891</u>
	<u>\$ 630,053</u>	<u>\$ 18,562</u>	<u>\$ 8,276</u>	<u>\$ 656,891</u>
<b>Reconciliation of operating income to net cash provided by operating activities</b>				
Operating income	\$ -	\$ -	\$ 43,123	\$ 43,123
Adjustments to reconcile operating income to net cash provided by operating activities:				
Changes in assets and liabilities:				
Unearned revenue	-	-	-	-
	-	-	-	-
Net cash provided by operating activities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 43,123</u>	<u>\$ 43,123</u>
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 43,123</u>	<u>\$ 43,123</u>

## **INTERNAL CONTROL AND COMPLIANCE**



**REHMANN ROBSON**

*Certified Public Accountants*

*A member of* **THE REHMANN GROUP**

 *an independent member of*  
**BAKER TILLY**  
INTERNATIONAL

**INDEPENDENT AUDITORS' REPORT ON  
INTERNAL CONTROL OVER FINANCIAL REPORTING  
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE  
WITH GOVERNMENT AUDITING STANDARDS**

April 7, 2008

The Board of Directors  
LifeWays  
Jackson, Michigan

We have audited the financial statements of the business-type activities, the major fund, and the aggregate remaining fund information of *LifeWays*, as of and for the year ended September 30, 2007, which collectively comprise *LifeWays*' basic financial statements as listed in the table of contents, and have issued our report thereon dated April 7, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered *LifeWays*' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of *LifeWays*' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of *LifeWays*' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described below to be significant deficiencies in internal control over financial reporting.

#### **Item 2007-1 - Preparation of Financial Statements in Accordance with GAAP**

<b>Criteria:</b>	All Michigan governments are required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). This is a responsibility of the government's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data (i.e., maintaining internal books and records), and (2) reporting government-wide and fund financial statements, including the related footnotes (i.e., external financial reporting.)
<b>Condition/Finding:</b>	As is the case with many smaller and medium-sized entities, the government has historically relied on its independent external auditors to assist in the preparation of the government-wide financial statements and footnotes as part of its external financial reporting process. Accordingly, the government's ability to prepare financial statements in accordance with GAAP is based, in part, on its reliance on its external auditors, who cannot by definition be considered a part of the government's internal controls.
<b>Cause:</b>	This condition was caused by the government's decision that it is more cost effective to outsource the preparation of its annual financial statements to the auditors than to incur the time and expense of obtaining the necessary training and expertise required for the government to perform this task internally.
<b>Effect:</b>	As a result of this condition, the government lacks internal controls over the preparation of financial statements in accordance with GAAP, and instead relies, in part, on its external auditors for assistance with this task.
<b>View of Responsible Officials:</b>	The government has evaluated the cost vs. benefit of establishing internal controls over the preparation of financial statements in accordance with GAAP, and determined that it is in the best interests of the government to outsource this task to its external auditors, and to carefully review the draft financial statements and notes prior to approving them and accepting responsibility for their content and presentation.

## **Item 2007-2 - Audit Adjustments**

<b>Criteria:</b>	LifeWays is responsible for the reconciliation of all general ledger accounts to their proper underlying balances for the purpose of creating a reasonably adjusted trial balance, from which the basic financial statements are derived.
<b>Condition/Finding:</b>	Audit procedures detected that the receivable and payable along with the related revenues and expenses for the Michigan Prisoner Re-Entry Program (MPRI) were materially misstated and required correction.
<b>Cause:</b>	LifeWays' internal controls did not detect all adjustments necessary to properly record year-end balances. A contributing factor to this was the fact the program is relatively new to LifeWays and was significantly expanded from previous years.
<b>Effect:</b>	As a result of this condition, material audit adjustments were necessary in order to properly recognize revenue and expense for the MPRI program.
<b>View of Responsible Officials:</b>	LifeWays recognizes the challenges associated with administering a new program like the Michigan Prisoner Re-entry through the Michigan Department of Corrections (MDOC), which is based on a reimbursable model, as opposed to the usual prepaid services model with the Michigan Department of Community Health (MDCH). In collaboration with key subcontractors and providers, LifeWays has convened a workgroup to document the business and operational flow to ensure that revenues and expenses are recognized in a timely and consistent manner during the period in which they were incurred.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 2007-2 to be a material weakness.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether *LifeWays'* financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of *LifeWays*, in a separate letter dated April 7, 2008.

*LifeWays'* responses to the findings identified in our audit are described above. We did not audit *LifeWays'* responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the audit committee, the governing board, management, others within the organization, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Lehmann Lobson". The signature is written in a cursive, flowing style with a large initial 'L'.





# REHMANN ROBSON

*Certified Public Accountants*

A member of THE REHMANN GROUP



April 7, 2008

To the Board of Directors of  
LifeWays  
Jackson, Michigan

We have audited the financial statements of LifeWays for the year ended September 30, 2007, and have issued our report thereon dated April 7, 2008. Professional standards require that we provide you with the following information related to our audit.

**Our Responsibility Under Auditing Standards Generally Accepted in the United States of America and Government Auditing Standards**

As stated in our engagement letter dated December 3, 2007, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal control of LifeWays. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of LifeWays' compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

**Significant Accounting Policies**

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by LifeWays are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by LifeWays during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

**Accounting Estimates**

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Management's estimate of the useful lives of depreciable capital assets is based on the length of time it is believed that those assets will provide some economic benefit in the future.
- Management's estimate of the liability for claims incurred but not reported.
- Management's estimate of its maximum risk exposure under its contract with MDCH. This estimate is the basis for determining whether the amount in the risk reserve internal service fund is within allowable limits.

We evaluated the key factors assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

**Audit Adjustments**

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on LifeWays' financial reporting process (that is, cause future financial statements to be materially misstated). We identified several audit adjustments, all of which were recorded by LifeWays, which in our judgment indicate matters that could have a significant effect on LifeWays' financial reporting process. As a result, we included a significant deficiency in our report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements in accordance with *Government Auditing Standards*.

**Disagreements with Management**

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

**Consultations with Other Independent Accountants**

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

**Issues Discussed Prior to Retention of Independent Auditors**

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as LifeWays' auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

**Difficulties Encountered in Performing the Audit**

We encountered no difficulties in dealing with management in performing our audit.

This letter and the accompanying memorandum are intended for the use of the Board of Directors, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink, reading "Lehmann Lohman". The signature is written in a cursive style with a large, stylized 'L' at the beginning.

# **LifeWays**

## **Comments and Recommendations**

**For the Year Ended September 30, 2007**

---

In planning and performing our audit of the financial statements of LifeWays as of and for the year ended September 30, 2007 in accordance with auditing standards generally accepted in the United States of America, we considered LifeWays' internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of LifeWays' internal control. Accordingly, we do not express an opinion on the effectiveness of the LifeWays' internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. The deficiencies we noted that we consider to be significant deficiencies are described in our report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with *Government Auditing Standards*.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 2007-2 to be a material weakness.

### **Other Matters**

#### **Credit Card Policy**

During the audit, we examined credit card statements from two different months throughout the year. Many of the expenditures on the card statements were not supported by a receipt or requisition form. The lack of original support for these expenditures increases the likelihood that assets could be misappropriated. LifeWays' current credit card policy is vague and does not address the types of purchases that are allowable and which employees are allowed to use the card. Instead, it refers to the purchasing policy which does grant certain employees (the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer) the power to approve purchases; however, it appeared as though many more employees were using the credit card. We recommend that LifeWays revisit its credit card policy and strengthen it by setting specific limitations on its use and requiring that receipts be retained to support these expenditures.

**LifeWays**  
**Comments and Recommendations (Concluded)**  
**For the Year Ended September 30, 2007**

---

**Review and Approval of Bank Reconciliations**

Effective internal control procedures should provide a clear trail of who performed what procedure and when. LifeWays is diligent in completing its bank reconciliations on a timely basis; however, the preparer does not initial and date the reconciliation to document the performance of the procedure. In addition, the reconciliations are not being independently reviewed and documented. We recommend that bank reconciliations be reviewed by a responsible official and both the preparer and reviewer should initial and date the document. We are pleased to note that management began this process with a retrospective review of the October and November 2007 bank reconciliations.

**Journal Entry Review**

During our review of internal controls over journal entry processes, we noted that while some journal entries were initialed or signed by someone other than the preparer as a check for journal entry completeness and accuracy, others were not. We again recommend that all journal entries be reviewed and initialed by an individual other than the preparer who is competent to understand that nature and purpose for the transaction.

**General Issues Regarding Cash**

During our audit, it was discovered that a bank account with a nominal amount of money had been closed, but the amount was still reflected on the trial balance. To ensure that this situation does not occur again in the future, we encourage management to implement a procedure for the closing of bank accounts and design it so that the appropriate individuals are notified of the closing. In addition, all bank accounts should be reconciled to the general ledger on a monthly basis.

We also noticed during our procedures that a check had been written and signed, but placed in the safe instead of being mailed to the vendor. The reason for not mailing the check that was given to us by management was the work had not been performed yet. However, the invoice related to this check had been accrued and included in capital asset additions, both of which are improper if the work had not been completed and the asset placed into service. We recommend that management eliminate the practice of writing checks to vendors before receiving an invoice.

\* \* \* \* \*